

**Before the
Federal Communications Commission
Washington, D.C. 20554**

In the Matter of)	
)	
)	CC Docket No. 96-45
Federal-State Joint Board on Universal Service)	

**Comments on Public Notice By The
Maine Public Utilities Commission And The
Vermont Public Service Board**

The Maine Public Utilities Commission and the Vermont Public Service Board are pleased to file initial comments in response to the Public Notice (“Notice”) released on August 17, 2005 relating to Proposals To Modify The Commission’s Rules Relating To High-Cost Universal Service Support.

I. GENERAL COMMENTS

A. Combining the programs

We applaud the fact that all of the proposals made in the Public Notice endorse or allow the provision of universal service support using a single system that is independent of the size or ownership characteristics of the incumbent local exchange carriers that historically have been serving rural customers. Maine and Vermont are two of a small number of states in which many rural customers are served by a large so-called “nonrural” provider. The existing support system for these “nonrural” carriers is highly dependent on the ability of these companies to make

implicit transfers of support from urban to rural areas. But without substantial urban areas, Maine and Vermont have little contribution base for such transfers.

Since 1993 we have been asserting in a series of FCC proceedings that distinctions based on carrier classifications (rural vs. nonrural or company size) have harmed consumers in Maine and Vermont. Originally, that discrimination arose from rules that explicitly provided more generous federal universal service support only for companies that had fewer than 200,000 lines, and especially generous support for companies with fewer than 50,000 lines. Currently, the discrimination is based on the distinction between “rural” carriers, as defined in the Communications Act, and other incumbent carriers. The new terms merely perpetuate the same problem, since we have minimal large urban areas and therefore have no greater ability than we did in 1993 to generate implicit subsidies from urban areas.

All four of the filed plans correctly recognize the desirability of moving to a single unified system.

B. Sufficient Support

The Tenth Circuit Court of Appeals has twice found that the FCC did not demonstrate that it has provided sufficient support to ensure that rates in rural areas are reasonably comparable to those in urban areas. After *Qwest I* was issued in 1991, the FCC took 27 months to deliberate the remand, and then it still did not meet the *Qwest I* standard. *Qwest II* was issued in February, 2005, seven months ago, and little action has been taken with regard to that remand. As some members of the Joint Board realize, the FCC must show that its universal service mechanisms provide sufficient support.

The support program at issue in *Quest II* was support provided to nonrural carriers. However, the Court’s rationale and conclusions apply to rural carriers as well. The Commission

must explain how its support programs relate to the statutory goals of comparable and affordable rates. All of the plans attached to the Notice either apply to both rural and nonrural carriers or could be made to apply to both classes of carriers.

II. COMMISSIONER BAUM’S “SAM” PLAN

Commissioner Baum’s Plan is largely derived from the Intercarrier Compensation Plan filed by the NARUC Intercarrier Compensation Task Force (“ICCTF”), Version 7. It, however, provides a more detailed procedural schedule for undertaking some of the work implied by the ICCTF plan.

We support the basic concept in the SAM proposal, that states should have direct control over distributions of federal universal service support. As universal service currently is defined, it is a federal program aimed at supporting local exchange rates. But those rates are set by state authorities. The FCC has no direct control over those rates, and has not even been able to develop a comprehensive and reliable way to measure and compare local rates.¹ To the extent that state commissions generally have more direct control than any other regulatory authority over local exchange rates, it makes sense for states to allocate universal service support.

Federal efforts to allocate support have suffered from serious methodological flaws and from insensitivity to local conditions. For example, the Commission was preoccupied for years with implementing support based on the use of forward-looking cost models, even though such models have no relationship to the rates actually paid by retail customers. Before that, the Commission designed the “DEM Weighting” program so that support was based exclusively on

¹ The FCC itself makes no effort to measure local rates in rural areas, only urban areas. Moreover, the methodology used in those studies ignores calling area scope, local option plans and bundling, and does not adequately measure the effects of usage charges.

the overall size of the company receiving the support; it provided support to high-cost and low-cost areas indifferently. Given those limitations, federal support has had limited effectiveness at actually lowering rates in the high-rate areas. All things considered, states are likely to do a much better job at allocating universal service funds where they are needed.

Another advantage of the SAM plan is that it allows states to make judgments about investment incentives. Currently the nonrural carriers receive support based upon an investment level that is hypothetically required in an idealized “forward-looking” network. Unlike rural carriers, they do not receive support based upon their actual investment. It is probably not a coincidence that rural carriers have deployed broadband far more widely than nonrural carriers. The SAM paper suggests that federal support to the states might ultimately be based on some statewide average FLEC cost. Even if this proves to be the case, states would still be free to *allocate* that support in ways that encourage desirable investment, and this could be an effective strategy to promote more rapid broadband deployment in many rural areas.

A. Problems With the SAM Plan

The SAM plan offers a detailed and thoughtful timetable for future decisions. However, it fails to address two important substantive issues. The first omission is so important that it renders the plan fundamentally incomplete.

1. Sufficiency of State Grant

Following *Qwest II*, the sufficiency of federal support is a critical issue for the Joint Board and the Commission. While the SAM Plan does recognize that support must be sufficient, it says nothing about what level of support is needed. To the contrary, it suggests a distribution mechanism that is likely to produce insufficient support.

The ICCTF Plan, Version 7, addressed the sufficiency issue by recommending a benchmark of 125 percent of urban cost. It provided:

8. After three years, the “permanent rate benchmark” should be set at 125% of the average urban rate, inclusive of interstate and intrastate SLCs and comparable mandatory charges. The rate benchmark should be used by the FCC as the basis for determining the need for universal service support after the initial three-year period.

ICCTF Version VII, at 11, filed in CC Docket No. 01-92. The intent was to ensure that no rural area would need to have rates more than 25 percent higher than the average urban area. This recommendation was the principal work product of the ICCTF’s work group on universal service. We believe the 125% benchmark is reasonable and meets the statutory standard for comparability.

Without explanation, the SAM plan deletes this important provision of the ICCTF plan. Instead, the SAM plan provides that a rate benchmark would be determined in the future, based upon identified factors and that this benchmark “could be used” by the FCC in distributing support.² It is not clear whether this “could” means “will,” or whether the FCC would have discretion to award support to states on some other basis.

Indeed, the SAM proposal suggests that some other basis, including historic payments, be used. Using “historical funding levels” would create a new state-based version of the “parent trap.” If past support levels are used to determine future support levels, then past inequities cannot be addressed. States that currently have many rural carriers and that receive generous support amounts would continue to receive those grants, not because they are needed, but because it is the status quo. That kind of distribution mechanism has nothing to do with the statutory goals of affordable and comparable rates.

² See SAM Plan at 4, ¶ 2; *see also* SAM Plan at 3 (method of allocating support to states “could be based on such factors as” a benchmark, among other things).

The SAM plan eliminates a critical element from the ICCTF that addressed the *Qwest II* mandate that the Commission demonstrate that its support is sufficient to satisfy Section 254.

Ten years after passage of the Telecommunications Act of 1996 and seven months after *Qwest II*, this is not an appropriate time to postpone defining the terms in the Act.

2. Sufficiency of State Allocations to Carriers

The SAM plan allows states to allocate funds provided to them as Federal USF support. However, Commissioner Baum's plan does not contain any mechanism to ensure that each carrier receives predictable and sufficient support so that it can offer services and rates comparable to those offered in urban areas. We believe that such a mechanism should be spelled out.

3. Separations

The SAM plan provides that federal support to states would be "nonjurisdictional."³ This simplifies the plan, but it does not address separations issues if a non-jurisdictional mechanism is not adopted by the FCC in the Inter-Carrier Compensation docket.

The ICCTF recommends a nonjurisdictional support mechanism, but it also attempts to resolve the associated separations issues. The ICCTF Plan, Version 7, provides that any state that sets rates for any incumbent LEC based on a revenue requirements analysis could:

do so on a total company basis. That is, it may set intrastate rates so that the LEC has an opportunity to earn a reasonable return on its intrastate and interstate operations, after considering all interstate revenues, including SLC revenues.⁴

Where a state commission retains regulatory authority over local and other intrastate rates, the Commission should define at least one approved separations mechanism by which it may set those rates if a unitary mechanism is not adopted for ICC. Moreover, as recommended in the

³ SAM Plan at 5.

⁴ ICCTF Version 7 at 14.

ICCTF Plan, that mechanism should be defined after consultation with the Separations Joint Board.

III. THREE-STAGE PACKAGE FROM MR. GREGG

In Stage 3, Mr. Gregg's plan's goal is very similar to that of the USERP plan proposed by Shifman, Bluhm and Pursley. However he proposes two intermediate steps.

A. Stage 1

In stage 1, he recommends consolidation of certain study areas and shifting the basis for measuring the costs of large carriers. Unfortunately, these intermediate steps may be so controversial and cumbersome that they may undercut the Commission's ability to reach the end point of the conversion to a unified mechanism. Therefore, we suggest transitioning to the final unified plan as quickly as possible without passing through this first stage.

Moreover, there seems little point in moving large rural carriers to a forward-looking cost model in Stage 1 if carrier support will finally be allocated by the states in Stage 3. State allocation decisions in Stage 3 might conceivably reverse changes made in Stage 1. There is little to be gained by using a forward-looking cost model for only a few years.

Mr. Gregg's Phase 1 commentary also suggests repeal of 47 C.F.R. § 54.305, the "parent trap." We support this action. While this rule was motivated by a desire to restrain the overall size of the fund, it has had pernicious effects. The majority of rural customers are served by so-called "nonrural" carriers. In states without large urban areas, these customers can have high rates, and the "parent trap" ensures that they cannot escape this problem even by sale of the incumbent to another, more legally favored, owner.

Mr. Gregg also would freeze per-line support upon competitive entry. This is his way of addressing the problem of increasing levels of support following entry for both the incumbent and the new entrant. However, this approach has significant disadvantages and may not comply with existing law. It means that universal service formulas could not respond to subsequent events or circumstance. A variety of events could affect the need for support, but the most obvious problem with frozen support is its inability to respond to natural disasters. A hurricane or similar event that destroys switching and distribution plant can substantially raise local exchange rates, and support should not be frozen for these customers.

A less dramatic problem with frozen support arises from the gradual effects of competition. While this frozen support proposal would protect contributors from paying more for universal service, it may not comply with existing law. Support limited by a per-line freeze amount may not provide sufficient support to maintain affordable and reasonably comparable rates as incumbent carriers lose lines to direct retail competitors and lose toll and access minutes to competing technologies.

States currently must review the comparability of rates in areas served by nonrural carriers and report their analysis to the Commission. Mr. Gregg suggests extending that obligation to cover rates charged by rural carriers. Collecting more data on rural and urban rates should help the Commission significantly in evaluating whether rates are reasonably comparable and affordable throughout the country and whether its support programs are providing support effectively to areas with high rates.

However, before the Commission extends further the current reporting obligations to cover the rates of rural carriers, it should make a significant effort to improve the validity of the existing rate reports. Existing measurement techniques are not well developed regarding local

measured service charges, local option packages or bundled services. Moreover, the measured rates make no effort to adjust for local calling area scope, although that is a prime predictor of local rates. Each of these factors reduces the reliability of the rate data that the Commission currently requires to be reported. Extending the existing system to rural companies could produce more data, but the Commission should first improve the validity of the existing data.

B. Stage 2

Mr. Gregg's Stage 2 proposal would combine several separate programs now used to support rural carriers. This is similar to the USERP plan, and we support it.

Mr. Gregg's Stage 2 proposal also incorporates for the first time a consideration of intercarrier revenues, something he calls a "revenue benchmark." This has several benefits. First, it is desirable to consider intercarrier revenues because they indisputably have an effect upon retail rates, and failure to consider those revenues could produce excess support. Second, it demonstrates the interdependence of universal service and intercarrier compensation mechanisms, and thereby provides a yardstick for estimating the universal service effects of any reform to intercarrier compensation. Third, it gives the commission a rationale to relate its cost-based support system to local rates, the touchstone in section 254. The essential nature of this relationship back to rates was confirmed as recently as February, 2005 by the Tenth Circuit in its *Qwest II* decision.

As in Stage 1, Mr. Gregg's Stage 2 plan creates dislocations as new support formulas are introduced. It is not clear why these conditions would be considered in any sense transitional. Rather, they could establish conditions that disappear upon adoption of Stage 3 and may create unnecessary adverse reactions. Moving directly to Stage 3, in measured steps, may be a more achievable method.

C. Stage 3

In Stage 3, Mr. Gregg's plan's goal is very similar to that of the USERP plan proposed by Shifman, Bluhm and Pursley. For the reasons given above, we support his recommendations that support be distributed by a unified system and that allocates support according to a "SAM" approach.

IV. THE HOLISTICALLY INTEGRATED PACKAGE OF COMMISSIONER NELSON

The Holistically Integrated Package ("HIP") submitted by Commissioner Nelson also has many similarities to the USERP plan.

The HIP plan supports the SAM grant system, subject to FCC guidelines. The HIP plan illustrates how differences among the states can legitimately lead to different preferences for support distributions. We support the Commissioner Nelson's observation that:

States are in a better position to ensure that USF funds are distributed to where they are needed because they are close to the customers and can provide the day-to-day oversight that is necessary to monitor potential abuse.

The HIP plan recognizes the importance of establishing a system not dependent upon the classification of the serving incumbent carrier. It recognizes that "support for high-cost rural areas should not be based on whether that area is served by a 'rural' or 'non-rural' carrier." We agree with this observation.

In addition, HIP includes a "permanent rate benchmark" of 125 percent of the national average urban rates. HIP correctly recognizes that any new universal service plan proposed at this time should include some basis to predict that it is likely to produce sufficient support to achieve reasonably comparable rates.

V. THE USERP PLAN

The USERP plan addresses the deficiencies we have identified in the other plans. USERP is a unitary plan that would provide sufficient support and that would help extend wireless service to unserved areas. It also uniquely offers a way to relate costs (and support based on costs) to “rates,” the statutory touchstone in section 254. By including a benchmark of 125 percent, USERP also makes it highly likely that support will be sufficient to ensure reasonably comparable rates in all areas.

Finally, USERP offers a sensible approach to supporting wireless carriers. This approach recognizes that buildout of wireless networks to rural areas should be a supported national goal. At the same time, the grant mechanism avoids the current problems, including upward pressure on the overall fund size as wireless carriers win customers from wireline carriers.

Respectfully submitted,

Patrick Damon
Administrative Director
Maine Public Utilities Commission
242 State Street
18 State House Station
Augusta, Maine 04333-0018

Gregg Faber
Utilities Analyst
Vermont Public Service Board
112 State Street, Drawer 20
Montpelier, Vermont 05620-2701

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